TCRS REPORT

SPECIAL TEACHERS' EDITION

Produced for active members of the Tennessee Consolidated Retirement System - Volume 20, No. 1 - Spring 1998

Steve Curry

From the Director...

Recently, there has been information disseminated about the TCRS plan, which unfortunately provides a misleading evaluation of the funding and benefit provisions of the TCRS.

Within this special newsletter we will provide you with information which is necessary to properly evaluate the benefits provided to teachers in Tennessee.

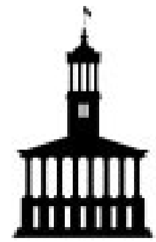
You will find that TCRS is a well managed retirement plan designed to provide benefits so that career employees are able to maintain their standard of living after retirement. Moreover, TCRS is funded on an actuarially sound basis so that current retirees and future retirees will feel assured that assets will be available to pay the benefits that have been promised.

Also within this publication, we will provide you with information about the second major benefit improvement enacted by the General Assembly within the last four years.

If you have any questions about the benefits and funded status of TCRS, please feel free to contact me. We are also available to meet with any group to review the TCRS plan. You can contact me by calling (615) 741-7063 or by writing to me at Tennessee Consolidated Retirement System, 10th Floor, Andrew Jackson Building, Nashville, Tenn., 37243.

Steven L. Curry

General Assembly Enacts Significant Benefit Improvement



During this last session of the General Assembly, legislation was enacted to provide for a significant benefit improvement by changing the methodology of the cost-of-living adjustment after retirement from simple to compound. This means that the annual COLAs will be computed on the most current benefit rather than the initial benefit at retirement.

The cost for this change exceeds $100 million annually. This increase is in addition to the 5% benefit improvement that was enacted in 1994 at an annual cost of more than $60 million. These two major improvements by the General Assembly represent a significant value to members of TCRS. The effect of a 3% compound COLA on your annual benefit is illustrated below:

Year of Retirement	No COLA	Simple COLA	Compound COLA
1st	$ 12,000	$ 12,000	$ 12,000
5th	12,000	13,440	13,506
10th	12,000	15,240	15,657
15th	12,000	17,040	18,151
20th	12,000	18,840	21,042
25th	12,000	20,640	24,394

This clearly shows the value of having an automatic COLA provision, especially one that is compound rather than simple.

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www.treasury.state.tn.us/tcrs.htm

TCRS Meets Benefit Objective

The objective of TCRS is to provide a level of benefits together with social security so that career employees can maintain their standard of living after retirement. An income replacement analysis is performed annually to determine if TCRS is meeting this objective. This comprehensive report can be obtained by calling or writing our office. This report is also available on our website.

The net income replacement ratio, after taxes and deductions, ranges from 88% to 105%. Based on this analysis, teachers with 30 or more years of service are able to maintain their same standard of living after retirement when considering income from two sources, TCRS and social security.

Comparison of Benefits 10 Years after Retirement

	Retirement System Benefit	Social Security Benefit	Total Pension Benefits
South Carolina	$ 24,327	$ 18,447	$ 42,774
Virginia	23,524	18,974	42,498
Arkansas	24,469	17,824	42,293
Tennessee	22,572	18,755	41,327
Florida	22,197	18,755	40,952
North Carolina	22,310	18,071	40,381
West Virginia	19,977	18,482	38,459
Alabama	19,597	17,954	37,551
Mississippi	20,411	17,109	37,520
Missouri	31,407	-	31,407
Georgia	28,870	-	28,870
Kentucky	28,823	-	28,823
Louisiana	21,125	-	21,125
Texas	20,317	-	20,317

This chart reflects the benefits on page 4, updated for annual changes in the CPI of an assumed 3%.

Separate Records Are Maintained for Each Group

Separate accounting and actuarial records are maintained for teachers as a group, state employees as a group, and employees of each individual local government participating in TCRS.

Every dollar contributed by teachers or on behalf of teachers plus the investment earnings on such contributions are used to pay benefits for teachers only.

Each of the three groups stand on their own and do not subsidize one another. Unfortunately, it has been cited incorrectly that teachers are paying for the benefits of the other groups. That simply is not factual.

TCRS is Strongly Funded

TCRS is a strongly funded plan, but not overfunded as some have suggested. Being strongly funded means that current retirees and future retirees should feel assured that the benefits which have been promised will be paid. Unfortunately, other states have not funded their retirement systems on an actuarially sound basis electing instead to push current pension cost onto future generations of taxpayers. The TCRS is being funded much like private sector pension plans. TCRS is not funded like social security and other federal pension plans which are only slightly better than pay as you go plans.

The Tennessee General Assembly has been recognized for its sound fiscal management of the pension program. Other states should be where Tennessee is relative to funding pension obligations. We certainly do not want to manage our obligations the way several states have. Obviously, those states which are deferring payments on their current pension costs are not exercising sound financial management, thus causing an even greater pension cost on their taxpayers. Ultimately, the delayed employer contributions plus the forfeited investment earnings will have to be paid. Tennessee is paying for the accrued pension cost for all employees on a current basis rather than pushing the cost to future generations of taxpayers.

Finally, if the plan were overfunded, the employer would not have to contribute the 6.5% of teacher salary that was contributed last fiscal year. Employer contributions were nearly $280 million. Since the plan is not overfunded, significant employer contributions must continue to be made to TCRS each year.

Retirement Benefits: Part of Employee Compensation Package

Retirement benefits should also be evaluated as part of the overall compensation package. According to NEA research, only two states in the southeast had average instructional staff salaries which exceeded Tennessee's during 1995-96. Salaries reported by NEA are shown on the chart on page 4.

Because Tennessee currently provides a higher level of compensation, the benefit formula at retirement is based on the higher level of compensation. Eight of the systems use a four or five year average salary for benefit calculation purposes, while six states use fewer years. Even though TCRS uses a five year average in the benefit formula, this average is higher than some of the other southeastern states which use less than five years. This is because of the higher level of compensation paid to Tennessee teachers.

State	Vesting	Credit for Sick Leave	Employee Contribution Rate
Arkansas	10 years	No	6.00
Alabama	10 years	Yes	5.00
West Virginia	5 years	Yes	6.00
Mississippi	4 years	Yes (Limited)	7.25
South Carolina	5 years	Yes (Limited)	6.00
North Carolina	5 years	Yes	6.00
Tennessee	5 years	Yes	5.00
Florida	10 years	No	0.00
Virginia	5 years	No	5.00
Kentucky	5 years	No	9.86
Missouri	5 years	No	10.50
Georgia	10 years	No	5.00
Louisiana	10 years	Yes	8.00
Texas	5 years	No	6.40

Actuarial Study Shows Gains

During the last session of the General Assembly, the budget for 1997-98 was amended by the legislature to provide for a benefit improvement and salary increase for teachers and state employees provided the June 30, 1997 actuarial valuation of TCRS reflected positive experience.

Fortunately, there were actuarial gains since the last actuarial valuation in 1995, mainly from investment earnings, which were utilized to provide for the compound COLA provision and to provide a salary increase. The employer contribution rate for teachers of 6.50% would have dropped to 2.32% but was set at 5.47% to finance the cost of the compound COLA. The remaining difference was utilized to grant a salary increase in January 1998.

The General Assembly, by its actions this last session, provided that any favorable decline in the employer contribution rate as determined by an actuarial valuation will be kept in the employee compensation package by improving benefits and / or increasing salary.

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Contributory vs. Noncontributory Issue

Teachers and state employees have the same benefits in TCRS. The eligibility requirements, the formula, post-retirement COLAs, death, disability, etc. are the same for both groups. It has been cited that teachers contribute 5% of salary to TCRS while state employees are noncontributory.

The reason for this difference relates to compensation. In 1981, teachers received a 7% across the board salary increase while state employees received a 2% salary increase plus elimination of the 5% contribution to the retirement system. These were equivalent monetary increases for both groups with the teacher increase costing slightly more due to matching social security cost.

Accordingly, state employees gave up or forfeited a salary increase in order to become noncontributory. Thus, noncontributory is a non-issue that is often raised because it is not understood.

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Comparing State Pension Benefits Is Complex Process

At this time, a comprehensive comparison of benefits of teacher retirement systems has never been compiled. An often cited NEA survey of benefit formulas compares only one of the numerous components of a retirement system. Relying on its limited analysis will cause incorrect interpretations because the NEA survey is not intended to be a comprehensive benefit comparison.

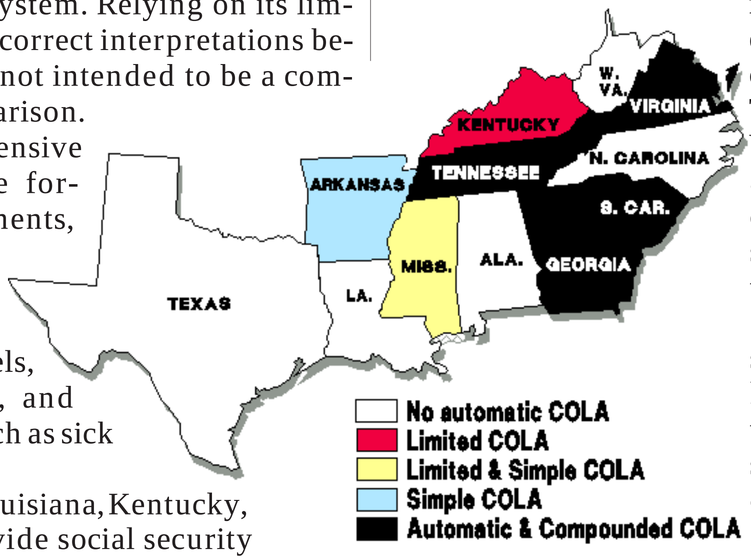
To perform a comprehensive benefit comparison, the formula, eligibility requirements, cost-of-living adjustments, vesting requirements, disability benefits, death benefits, salary levels, social security coverage, and credit for other service such as sick leave must be included.

Many states such as Louisiana, Kentucky, and Missouri do not provide social security coverage for employees as Tennessee does. States which do not provide social security coverage provide, as they should, a somewhat higher benefit formula.

Therefore, it is misleading to conclude that states without social security coverage provide better benefits, when in fact the combination of the TCRS benefit and social security exceeds the benefits in those states where social security is not provided.

Many states do not have automatic cost-of-living adjustments (COLA) after retirement, while Tennessee has a 3% CPI based COLA. For example, Alabama, West Virginia, North Carolina, Louisiana, and Texas do not provide automatic CPI based COLAs. Moreover, Kentucky has a maximum annual cap of 1.5% while Mississippi's cap is 2.5%. The COLA in Arkansas and Mississippi is simple rather than compound. To disregard one of the most important features of a retirement plan, such as COLAs, will cause an invalid assessment of a retirement plan.

Tennessee has a vesting period of five years while four states in the southeast use 10 years. Teachers contribute 5% of salary to TCRS. In Arkansas, West Virginia, South Carolina, and North Carolina, the employee rate is 6%. Mississippi requires teachers to contribute at 7.25%.



In many states, it is not the state that is paying for a higher level of benefits but the teacher. A program should be evaluated based on the employer-provided portion of a benefit. Tennessee grants service credit for unused accumulated sick leave, yet seven states in the southeast do not. The pensions of seven states in the southeast are subject to a state income tax while the TCRS is not.

Comparison of Pension Benefits in Southeastern States

State	1995-96 Average Salary	Retirement System Benefit	Social Security Benefit	Total Pension Benefits	Benefits as a % of Salary	Is Pension Subject to State Income Taxes?
West Virginia	$33,296	$ 19,978	$13,779	$33,757	101%	Yes
Alabama	32,459	19,597	13,637	33,234	102%	No
Arkansas	30,607	18,823	13,280	32,103	105%	>$6,000
South Carolina	33,155	18,103	13,765	31,868	96%	Yes
Virginia	35,535	17,506	14,129	31,635	89%	Yes
Tennessee	34,412	16,796	13,979	30,775	89%	No
Florida	34,411	16,517	13,979	30,496	89%	No
North Carolina	31,622	16,602	13,480	30,082	95%	>$4,000
Mississippi	28,712	16,330	12,770	29,100	101%	No
Kentucky*	33,115	24,836	-	24,836	75%	No
Missouri*	33,870	23,370	-	23,370	69%	Yes
Georgia**	35,804	21,482	-	21,482	60%	Yes
Lousiana*	28,167	21,125	-	21,125	75%	No
Texas**	33,861	20,317	-	20,317	60%	No

* No Social Security Coverage

** Social Security coverage determined by each individual school system.

Assumptions: 30 years of service
1995-96 salary based on average salary of instructional staff